In the Supreme Court of the United States

OCTOBER TERM, 1972

No. 72-1308

NORMAN SHUTLER AND VIRGINIA SHUTLER;
A. H. TURNER AND EDITH TURNER, PETITIONERS

v.

UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT

MEMORANDUM FOR THE RESPONDENT IN OPPOSITION

Petitioners claim that they are entitled to deduct from their gross income for the year 1966 amounts expended in acquiring a leasehold in a quarter section of agricultural or grazing land owned by the State of Oklahoma. The record in this case, based upon fully stipulated facts, does not support petitioners' claim. The decision below is correct. There is no conflict of decisions or any other ground for further review.

Petitioners, co-tenants in farming operations in Oklahoma, purchased at an estate auction a leasehold in agricultural or grazing land owned by the State of Oklahoma and supervised by the Oklahoma State Land Office. They paid for the lease a total of $15,000, of which $13,000 was allocated to the cost of acquiring the lease and $2,000 to improvements.

The annual rent, set by the Land Office, was $850. Upon petitioners' purchasing the lease, the estate, pursuant to the requirements of the Land Office, executed a relinquishment in favor of the petitioners, who thereafter made formal application for and obtained the lease for its remaining period of less than five months, and subsequently for an additional lease period. (Pet. App. 11-13.)

The Oklahoma State Land Office enters into many agricultural and grazing leases, all of which run concurrently for five-year periods. Under those designated "preference right leases," such as the one in the instant case, the state contractually grants the lessee the preferential right to purchase the land for an amount equal to the highest bid, if and when the land is sold. However, in practice these lands have almost never been sold; instead, the lessee is given the right to re-lease the land indefinitely upon expiration of each lease period. (Pet. App. 13.)

Section 162 of the Internal Revenue Code of 1954 allows a taxpayer to deduct from gross income all the ordinary and necessary business expenses incurred in carrying on his trade or business during the taxable year. This Court's decisions have established that the ordinary and necessary business expense deduction does not include capital expenditures (*Welch* v. *Helvering*, 290 U.S. 111), and that an expenditure that results in the acquisition of an asset having a useful life of more than one year, such as a leasehold for a term longer than a year, should be treated as a capital expenditure (*Commissioner* v. *Lincoln Savings & Loan Assn.*, 403 U.S. 345, 352, 354; *United States* v. *Catto*, 384 U.S. 102, 109; *Deputy* v. *duPont*, 308 U.S. 488). Furthermore, although the cost of a lease

may often be amortized over its term (Treasury Regulations on Income Tax (1954 Code) §1.162-11, cited by taxpayer, Pet. 5), when that term can be determined with reasonable certainty (Section 178 (c), Internal Revenue Code of 1954), a lease or other asset which is reasonably certain to be renewable for an indefinite period may not be amortized. *Nachman* v. *Commissioner,* 191 F. 2d 934 (C.A. 5); *KWTX Broadcasting Co.* v. *Commissioner,* 272 F. 2d 406 (C.A. 5); *Commissioner* v. *Indiana Broadcasting Corp.,* 350 F. 2d 580 (C.A. 7); and *Richmond Television Corp.* v. *United States,* 354 F. 2d 410 (C.A. 4).

Here the court of appeals, on the basis of the stipulated Rules and Regulations of the Commissioners of the Land Office, concluded that it was the policy and the unvarying practice of that office, carried out in this case, to renew indefinitely these five-year leases of agricultural and grazing lands. Accordingly, the court held that petitioners were not entitled to deduct the cost of acquiring the lease in the year of acquisition.[1] The court's holding with respect to that factual determination does not require further review.[2]

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[1]Indeed, though the point was not directly in issue, the court's holding would also preclude petitioners from amortizing the cost of acquiring the leasehold over the original period plus the first five-year renewal period, on the ground that petitioners could, and were likely to, continue to renew the lease indefinitely.

[2]Petitioners' reliance upon *Scully* v. *United States,* 409 F. 2d 1061 (C.A. 10), is misplaced, since that case turns on technical principles used in condemnation suits to determine the value of a leasehold interest, rather than on the principles applied under federal tax statutes to determine whether an expenditure is for the acquisition of a capital asset.

The petition for a writ of certiorari should be denied.

Respectfully submitted.

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